APPENDIX I

United States District Court
Northern District of Georgia
Rome Division

The Day Companies,
Plaintiff,
vs.
Claud T. Patat, Jr., John L. Farris and Patat Plywood Corp.,
Defendants.
Civil Action.
Number 1945.

This is an action for breach of a covenant not to compete entered into by the defendant Farris in connection with the sale of his plywood business to plaintiff. The particular covenant in question provides:

> "(6) John L. Farris, individually, agrees to remain in the employ of Farris until December 31, 1966, at a salary of Five Hundred and 00/100ths Dollars ($500.00) per month in an advisory and consulting capacity, it being understood that he shall not be required to keep regular hours or perform any detailed administrative or executive duties; the said John L. Farris, individually, further agrees that during the term of his said employment, and for a period of five (5) years thereafter (that is, until December 31, 1971) he will not, either directly or indirectly, alone or in concert with any other person, firm or corporation, be connected with or concerned in any business or employment which shall be in competition with Farris in the area presently operated in by Farris."

In a ruling on summary judgment on February 1, 1968, this court held the covenant valid as to "time of restraint." On appeal, the Fifth Circuit held the covenant valid as to "definiteness as to the nature, kind and character of the activities prohibited by the contract." **Day Companies v. Patat,** 403 F.2d 792 (5th Cir. 1968), **cert. den.** 397 U. S. 1117 (1969). It likewise held that the covenant was not invalid on its face for want of "definiteness and reasonableness as to the territory involved."

Following discovery and denial of summary judgment, the injunctive feature of the case came on for trial before the court. At issue is the meaning of the phrase "in competition with Farris in the area presently operated in by Farris." Such question is necessarily dependent upon the evidence, on which the court makes the following

FINDINGS OF FACT

In 1949 E. O. Dulaney of Louisville, Kentucky was president of General Plywood Corporation and John L. Farris was a vice-president and general production manager at its Savannah, Georgia, facility. At that time, Dulaney determined to go into business for himself and he formed the Dulaney Veneer Company at Cuthbert, Georgia, and employed Farris to be vice-president and general manager. Dulaney was apparently knowledgeable in the matter of plywood marketing nationally and he also created one or more sales corporations in Louisville, for such purpose, the principal one being known as Dulaney Plywood Corporation. Farris was strictly a production man in the industry and had sole charge of the Cuthbert plant for Dulaney. The combination of the talents of the two was apparently ultra-successful and for ten years the business flourished with the orders being obtained by Dulaney Plywood in Louisville and executed by Dulaney Veneer in Cuthbert. By the end of that period, the principal prod-

uct manufactured was "doorskins", which are plywood panels used for the fabrication of wooden doors by various door companies throughout the United States.

In 1959, partly to reward Farris for an outstanding job over the years, Dulaney sold the Cuthbert plant to him on very favorable terms to be satisfied, in the main, out of future profits. To effect the transfer, the Farris Plywood Company, Inc. was created, in which Farris and his family were the sole stockholders and it took over all of the physical assets of the Cuthbert plant. Dulaney continued to handle all of the marketing problems through the Dulaney Plywood Corporation in Louisville.

The actual method of operation was as follows: Dulaney Plywood would obtain an order from the trade and relay the requirements to Farris Plywood. Farris Plywood would execute the order and ship direct to the customer, invoicing Dulaney Plywood. Dulaney Plywood would remit to Farris Plywood and collect from the customer. With very minor and insignificant local sales, all of Farris Plywood's production was sold in this manner, and it manufactured only on order, maintaining little if any stock. All in all, Farris "counted on Dulaney to keep him going." During the period of 1959-1966, Farris Plywood had no salesman and the retail prices were all set by Dulaney. Conversely, Dulaney Plywood had no other source of "doorskins" except Farris, and maintained no warehouse or other storage facility for them. In 1959, Claud T. Patat was foreman of the Cuthbert Dulaney plant under Farris and was made vice-president of Farris Plywood on the change-over.

Early in 1966, Columbus Packing Company (the predecessor to plaintiff here, The Day Companies), a Mississippi plywood manufacturer, initiated inquiries through Jameson Investment Company of Birmingham, looking toward a merger with or purchase of Farris Plywood

Company. Following the initial contact, the negotiations were handled principally by Clarence C. Day, President of Columbus Packing and Farris for Farris Plywood. Upon agreement in principle at a total price of some $465,500 by those two, a meeting was arranged at Montgomery, Alabama, between them along with attorneys for the purpose of discussing the terms of the formal purchase agreement.

Prior to the meeting, Farris had a draft of a proposed contract prepared by his attorney, Jessie Bowles (D-3). Paragraph 6(d) provided: "The corporation will continue the verbal agreement presently existing between the corporation and Dulaney Plywood Corporation of Louisville, Kentucky, wherein the latter corporation is to handle the sale and marketing of products of Farris Plywood Company as heretofore, through the 1st day of October, 1966."

At the Montgomery meeting, another draft prepared by W. J. Threadgill as attorney for Day was presented and discussed paragraph-by-paragraph by the two principals and attorneys Bowles and Threadgill. This draft eventually became the basis of the executed contract (Exhibit "A" to amended petition). The draft proposal (D-2) provided in Paragraph 6 as follows:

> "(6) John L. Farris, individually, agrees to remain in the employ of Farris until December 31, 1966, at a salary of Five Hundred and 00/100ths Dollars ($500.00) per month and to perform such duties during said period for Farris as its board of directors may reasonably prescribe; the said John L. Farris, individually, further agrees that during the term of his said employment, and for a period of five (5) years thereafter (that is, until December 31, 1971) he will not, either directly or indirectly, alone or in concert with any other person, firm or corporation, be connected with or concerned in any business or employment which shall be in competition with Farris, and

during the aforesaid period of employment shall use his utmost endeavors to promote the business and the interests of Farris."

Considerable discussion surrounded this provision, Day insisting that he was "Not interested in buying if Farris didn't quit," but that he wanted him to continue for a reasonable period within the company. On the other hand, Farris stated he wanted to quit and had no intention of going back into business. Because of the technical requirements of Georgia law regarding non-competing covenants, the wording of Paragraph 6 was examined at length and various suggestions such as "the whole United States" were injected by the lawyers. The area of logging and labor supply around Cuthbert was also discussed. At the suggestion of Attorney Bowles for Farris, paragraph 6 was changed to read:

"(6) John L. Farris, individually, agrees to remain in the employ of Farris until December 31, 1966, at a salary of Five Hundred and 00/100ths Dollars ($500.00) per month in an advisory and consulting capacity, it being understood that he shall not be required to keep regular hours or perform any detailed administrative or executive duties; the said John L. Farris, individually, further agrees that during the term of his said employment, and for a period of five (5) years thereafter (that is, until December 31, 1971) he will not, either directly or indirectly, alone or in concert with any other person, firm or corporation, be connected with or concerned in any business or employment which shall be in competition with Farris in the area presently operated in by Farris."

At the meeting, Day discussed for the first time the nature of the sales arrangement with Dulaney. He thereupon insisted that it be continued so that he could receive payment on a weekly basis. Farris stated that Dulaney

handled "our established accounts" and that Farris customers were located "from New York to Texas." The provision regarding Dulaney was amended to provide:

> "Farris will continue the verbal agreement presently existing between said corporation and Dulaney Plywood Corporation, Louisville, Kentucky, with respect to the sale and marketing of products of Farris, until the first day of October, 1966, which said agreement is as follows: Sales to established accounts heretofore sold through Dulaney shall continue to be made through Dulaney, but at prices established by Farris."

Prior to execution of the contract, Farris revealed the proposal to Dulaney and received his approval to proceed as outlined.

The contract as finally executed on April 20, 1966, also provided for the continued employment of Patat for the remainder of 1966 at $1,000 per month plus a $10,000 year-end bonus (Par. 3a).

For some six months following the sale, the new owners operated through Dulaney Plywood as before with the same modus operandi as used previously. In September, Day undertook to terminate the arrangement between Farris Plywood and Dulaney Plywood and sent a new Farris vice-president, Norsworthy, to Louisville for that purpose. Dulaney became upset at this prospect and, as a result, Farris came to Louisville to enter the discussion. The upshot of the meeting was the formulation of an agreement by Norsworthy, Dulaney and Farris to buy out the Dulaney sales organizations (P-9), on condition that Dulaney and certain key employees be granted future employment contracts. On September 20, 1966, Farris Plywood under the new owner, executed such an arrangement (P-8), and in 1967 the name was changed to Farris Plywood.

Farris terminated all his connections with Farris Plywood on December 31, 1966, and Patat terminated his

employment there in mid-January, 1967. Patat considered several business possibilities and in February, 1967, decided to go into the doorskin business himself. As a friend, he discussed the matter with Farris and told him he was going to approach the Small Business Administration for a loan for such purpose. Upon refusal of the loan he again talked with Farris—this time with a view toward obtaining the backing of Farris in the venture. In the discussion, Patat was shown the sales contract with Columbus Packing, including specifically the non-competing covenant in question. After consultation with an attorney, it was decided that the covenant only had reference to the Cuthbert trade and logging area. Contact made by Patat with the Rockmart Chamber of Commerce, resulting in a favorable plant-arrangement there, some 175 miles from the Cuthbert plant. On this basis, the Patat Plywood Corporation was organized with Patat owning 250 shares and Farris owning another 250 shares of its capital stock in March, 1967. Patat was named as President and Farris as vice-president and treasurer. In addition, Farris (and his wife) loaned the corporation $100,000 on a demand note, secured by the new company's equipment. Immediately upon operation it began producing "doorskins" similar to those produced by Farris. Patat and Farris actively solicited customers formerly shipped by Farris through Dulaney and by January, 1968, substantially all of Patat's production was being purchased by the Wall Lake Door Company, a former major purchaser of Farris' production of birch "doorskins."

Following the filing of this suit, Farris sold his capital stock in Patat Plywood to Patat for $25,000, and resigned as an officer, director, and employee in December, 1968. He still holds the demand notes for $100,000, but neither he nor any member of his family has any other connection with or participation in the company nor has he engaged in any activity for the company since that time.

Patat and the Patat Company knew of the provisions of the covenant prior to beginning production and each was a beneficiary of Farris' activities thereafter.

CONCLUSIONS OF LAW

Construction of the covenant.

The court is of the opinion that this controversy arose over a situation completely unforeseen by the parties or their attorneys at the time of negotiations and sale. The business conflict which has developed was unanticipated by any of them at that time and, consequently, the contract language employed does not define the non-competing area with particularity nor does it clarify the meaning of "operations" by Farris, considering its unique arrangement with Dulaney. While the subsequent Farris-Patat venture appears not to have been contrived, nonetheless, it is clear that the parties are bound by their contract and, the Fifth Circuit having held that the covenant is enforceable, it devolves upon this court to place a proper legal construction upon it.

Considering the binding nature of the contract, the posture of the parties is one of complete apposition. Recognizing the significance of the Dulaney arraignment, the plaintiff contends that the covenant extends to the reasonable trade area of each consumer shipped by Farris, while the defendant contends that Dulaney Plywood was, in legal terms, its only customer, and that the area covered by the covenant is limited to the supply and labor area of Cuthbert. While the conversation at Montgomery appears to have been primarily directed to the nature of the Cuthbert area, the simple expedient of describing it was rejected and broader language employed. The court concludes, whether mutually intended or not, that the covenant in fact includes more, particularly in view of the

announced policy of the Georgia courts to give wider latitude to such restrictions in the case of a sale of a going business. **Day Companies v. Patat**, 403 F.2d 792 at 795(7), citing **Strauss v. Phillips**, 180 Ga. 641, **Morris-Forrester Oil Co. v. Taylor**, 158 Ga. 201, and **Legg v. Hood**, 154 Ga. 28.

Solution of the problem thus gets down to a reasonable view of the Dulaney arrangement. Its existence and true nature was well known to the parties at the time, as evidenced by the testimony and the language employed in the contract (See paragraphs 2 j and 3 d). Neither counsel nor the court can find a satisfactory legal label to describe the Dulaney arrangement. In a traditional commercial relationship, none of the possibilities from which some semi-automatic answer could be fashioned, such jobber, wholesaler, retailer, factor, or even customer, seem appropriate. In most respects it is most akin to that of a "sales agent." See **F. P. Williams Co. v. Colorado Milling and Elevator Co.**, 246 F.2d 240 (5th Cir. 1957); **Etablissements Rigaud v. Hoey**, 50 F. Supp. 598 (S.D.N.Y. 1942). However, most ordinary sales agents do not assume the financial risk of the consumer as here.

In such matters, the watchwords should be the "commercial realities" and "economic significances" of the factual situation. **Brown Shoe Co. v. United States**, 370 U. S. 294 at 325 (1961). In truth, the arrangement was a paternalistic supervision of his own creation by Dulaney, who doubtless wished for Farris to prosper over and beyond repayment of the purchase price. In any view of such a situation, the court can only conclude that Dulaney's customers were Farris' customers and vice-versa, as the former had no production and the latter no market without the other. Viewed from the strict posture of "trade area", the two coincide as Dulaney's trade area from Louisville encompasses the same users as shipped by Farris from Cuthbert.

If the covenant is to be given any viable meaning over and beyond the Cuthbert supply area, and it must, the commercial reality is that plaintiff be afforded protection in the sense that Dulaney's operations are, in fact, Farris' operations, and Dulaney's customers are, in fact, Farris' customers. Such is the ruling of the court.

Remedy

While the prohibition against Farris personally is absolute, as to the Patat Company, the plaintiff recognizes that in construing the territorial limits of the restraint, the restriction should be what is reasonably necessary for the protection of the business acquired. 43 C.J.S., **Injunctions** § 84. E. g. **Thomas v. Coastal Industries, Inc.**, 214 Ga. 832 (1959); **National Homes Corp. v. Lester Industries, Inc.**, 293 F. Supp. 1028 (W.D. Va. 1968). And reasonableness depends upon the facts and circumstances of each particular case. Here, there is no need to describe geographical areas, for the nature of the business is not to serve a geographic market, but a customer market. All that is needed in this respect for plaintiff's protection is relief as to customers. That is the true area in which Farris formerly operated and Patat now does. It is not unlike an unfair competition claim against the solicitation of former customers as a part of good will purchased. See 38 C.J.S., **Good Will**, § 7 ff. Thus, for example, it is reasonable to prohibit solicitation or sale to an existing customer in Houston, Texas, but it is not reasonable to prohibit solicitation or sale to a new or competing customer in the entire Houston trade area.

Accordingly, the direction of the court will be to enjoin the defendant Farris personally from engaging, directly or indirectly, in any capacity, in any business or employment in competition with Farris and specifically with the other defendants,[1] and to enjoin all of the defendants jointly

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[1] Plaintiff insists also that defendant Farris should be directed to call his loan to Patat Corporation, so as to divest his

from selling or soliciting any former Farris customers. Customers are defined as those purchasers named on Plaintiff's Exhibit 5 at trial, excepting therefrom:

Manhattan Door, Mespeth, L. I., N. Y.;
Boro S. W. Corp., Fort Worth, Texas;
Georgia Pacific, Orlando, Florida;
Hurd Millwork Corp., Medford, Wisconsin;
U. S. Plywood, Laurel, Mississippi,

all of whom were sold by Farris Plywood following the date of sale.

In order to afford defendants a reasonable opportunity to adjust to business necessities, such relief will be effective on September 1, 1970, and extend through the life of the contract. An order may be presented by plaintiff's counsel to such effect. The claim for damages is deferred for jury trial as agreed.

It Is So Ordered.

This the 13th day of July, 1970.

/s/ SIDNEY O. SMITH, JR.
SIDNEY O. SMITH, JR.
United States District Judge

Filed in clerk's office and a true copy certified, this July 14th, 1970.

CLAUDE B. GOOD
Clerk

By: DAN DAVIS
Deputy Clerk

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connection therein. The court is convinced that Farris has, in fact, divorced himself from any active participation in the business as of December, 1968, and the court does not consider the position of creditor to be in violation of the covenant. Therefore, such relief will not be granted. Any action by Farris on behalf of the corporation would, however, constitute a violation of the order and, if shown, would subject him to sanctions for contempt, even if it were arguably motivated to strengthen his loan position.

APPENDIX II

In the
United States Court of Appeals
For the Fifth Circuit

No. 30415

The Day Companies, Inc.,
Plaintiff-Appellee,

versus

Claud T. Patat, Jr., John L. Farris
and Patat Plywood Corporation,
Defendants-Appellants.

Appeal from the United States District Court for the
Northern District of Georgia

(April 16, 1971)

Before Brown, Chief Judge, Coleman and Clark,
Circuit Judges.

Per Curiam: This is the second appearance of this case in this Court. Our prior decision is reported, 1968, 403 F.2d 792.

In a carefully considered opinion it was there held by a panel of this Court that a contract from a seller not to compete with his buyer was valid under Georgia law. The covenant not to compete was expressed in the following language:

> "the said John L. Farris, individually, further agrees that during the term of his said employment, and for a period of five years thereafter (that is, until December 31, 1971) he will not, either directly or indirectly, alone or in concert with any other person, firm or corporation, be connected with or concerned in any business or employment which shall be in competition with Farris in the area presently operated in by Farris." 403 F.2d 793.

After remand, and upon trial to the merits, the parties vigorously disagreed about the meaning and extent of the covenant language, "*in the area presently operated in by Farris*".

Mr. Farris claimed that it was intended to apply only to his previously existing logging operations in and around Cuthbert, Georgia.

Day argued, of course, that the noncompetitive protection extended to former customers who bought Farris products and to the area in which they operated. There was much argument below, and here, as to whether Dulaney Plywood Corporation, through whom Farris made its sales, was a customer or a jobber or a wholesaler or a factor.

We think this issue was covered by what we said in the prior opinion:

> "Considering the challenge as to the territory prerequisite, was this covenant reasonable and definite as to the area involved here? The limitation in the covenant as to territory in the case at hand is found in the phrase 'in the area presently operated in by Farris'. The cases from the Georgia Courts seem to permit restraints which extend throughout the territory covered by a transferred business. As was ob-

served by Judge Jenkins of the Georgia Supreme Court in Kutash v. Gluckman, 193 Ga. 805, 20 S.E.2d 128 'a contract which affords a fair protection to the party in whose favor it is made, and is not injurious to the public * * * may extend to all the territory covered by the business the good will of which has been sold * * *'. We agree with the Court below that the standard of area is met in the agreement in question." 403 F.2d 794.

The District Court, upon remand, from which this appeal was taken, held that the covenant applied to all those customers who were purchasing manufactured goods produced by Farris at the time he sold the business. It seems clear to us that Day was entitled to that much relief, if not more. There is no cross appeal from the failure to include sales in the territorial areas occupied by these customers, so we intimate nothing on that point.

Claud T. Patat, Jr. and Patat Plywood Corporation argue that no injunctive relief should have been granted against them as they were not parties to the original contract. Nevertheless, there was evidence in the record to support the finding of the District Court that the Patats have knowingly been in complicity with Farris in violation of the contract not to compete.

There was no error below. The judgment of the District Court is

AFFIRMED

APPENDIX III

United States Court of Appeals
For the Fifth Circuit

October Term, 1970

No. 30415

D. C. Docket No. CA 1945
The Day Companies, Inc.,
Plaintiff-Appellee,
versus
Claud T. Patat, Jr., John L. Farris
and Patat Plywood Corporation,
Defendants-Appellants.

Appeal From the United States District Court for the Northern District of Georgia
Before Brown, Chief Judge, Coleman and Clark, Circuit Judges.

Judgment

This cause came on to be heard on the transcript of the record from the United States District Court for the Northern District of Georgia, and was argued by counsel;

On Consideration Whereof, It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, affirmed.

It is further ordered that defendants-appellants pay to plaintiff-appellee, the costs on appeal to be taxed by the Clerk of this Court.

April 16, 1971

Issued as Mandate: